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Amendment to Extensions of auditing procedure; Statements on auditing procedure, No. 12

American Institute of Accountants. Committee on Auditing Procedure

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Statements on Auditing Procedure

No. 12

October 1942

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American Institute of Accountants,
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Amendment to Extensions of Auditing Procedure

FOREWORD

IN MAY, 1942, the committee on auditing procedure of the American Institute of Accountants issued a supplementary report to the council in which the committee recommended an amendment to the report, "Extensions of Auditing Procedure," approved at the annual meeting of the Institute on September 19, 1939.¹ The council approved this supplementary report with the understanding that it would subsequently come before the annual meeting of the Institute. It was presented at the annual meeting in Chicago on October 1, 1942, and was formally approved. The report follows.

SUPPLEMENTARY REPORT OF THE COMMITTEE ON AUDITING PROCEDURE

On September 19, 1939, at the annual meeting of the American Institute of Accountants, the membership approved suggestions of the special committee on auditing procedure as to extensions of auditing procedure, particularly with regard to examination of inventory quantities and confirmation of receivables, contained in a report entitled "Extensions of Auditing Procedure."

The report also discussed certain phases of the independent public accountant's report or opinion. It stated, in part, as follows:

"It is the responsibility of the accountant—and one which he cannot escape—to determine the scope of the examination which he should make before giving his opinion on the statements under review. If in his judgment it is not practicable and reasonable in the circumstances of a given engagement to undertake the auditing procedures regarding inventories and/or receivables set forth in this report as generally accepted procedure and he has satisfied

¹ Statements on Auditing Procedure No. 1.

Statements on Auditing Procedure

himself by other methods regarding such inventories and/or receivables, no useful purpose will be served by requiring an explanation in his report. If physical tests of inventories and/or confirmation of receivables are practicable and reasonable and the auditor has omitted such generally accepted auditing procedure, he should make a clear-cut exception in his report."

The second sentence of this paragraph made unnecessary the disclosure of the omission of certain normal procedures when in the accountant's judgment they are not practicable and reasonable and when he had satisfied himself by other methods.

The committee on auditing procedure believes that there was considerable merit in the philosophy underlying this statement; it placed full responsibility on the independent public accountant and emphasized the necessity of users of financial statements relying on the professional judgment, skill, and reputation of the practitioner making the particular examination. In those cases in which application of the extended procedures was not practicable and reasonable, it also avoided the casting of what might appear to be an unwarranted cloud upon the financial statements.

The fact that disclosure was not required, however, has given rise to widespread misunderstanding, and especially so since the Securities and Exchange Commission in its amended rule² regarding accountant's "certificates" made such disclosure mandatory in all reports filed with the Commission. The difference in the two requirements has given the appearance of different standards as between listed and unlisted companies.

This impression is unfortunate in view of the fact that many, if not the majority, of practitioners follow the Commission's rule in all cases regardless of whether listed or unlisted companies are involved. In Bulletin No. 6, issued in March, 1941, which dealt with the new Commission rule, the committee stated:

"The revised rule is, of course, applicable only to reports filed with the Commission. As a practical matter, however, practicing accountants may in course of time consider it advisable to apply the same standards of disclosure in reports for other purposes also, though the old form will doubtless continue to be used for an intermediate period."

The committee feels that the profession, to a substantial extent, has already adopted the new standards of disclosure and that the present Institute rule no longer is in agreement with the more common practice.

² Rule 2-02 (b) (i) of Regulation S-X, as amended.

Amendment to Extensions

It has also become increasingly evident since the issuance of "Extensions of Auditing Procedure" that relatively few cases exist in which the application of the normal procedures with respect to inventories and/or receivables is not practicable and reasonable, so that the considerations which gave rise to the original rule are in large measure inapplicable.

Accordingly, the committee on auditing procedure hereby recommends that hereafter disclosure be required in the short form of independent accountant's report or opinion in all cases in which the extended procedures regarding inventories and receivables set forth in "Extensions of Auditing Procedure" are not carried out, regardless of whether they are practicable and reasonable, and even though the independent accountant may have satisfied himself by other methods.

May 1, 1942

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